

Solving the efficiency conundrum for ETDs (Exchange Traded Derivatives)

Centrally matching futures and options using FIX



Post-trade processing is a critical – albeit often overlooked – component of the trade lifecycle. Efforts to accelerate automation in areas such as trade matching, confirmation and allocation have been ongoing for many years, however a number of asset classes including ETDs, remain a challenge for the industry.

Broadridge provides its unique insights into how asset managers can obtain major efficiencies through better post-trade automation.

POST-TRADE AUTOMATION: A MULTI-YEAR JOURNEY

Historically, the majority of the post-trade cycle of an institution's equities workflow have been carried out using a single provider, which has been the only organisation in the market to offer acceptable levels of automation.

In 2013, the FIX Trading Community announced the establishment of the Global Post-Trade Working Group, a body comprised of industry leaders from the Americas, Europe and Asia. The group was tasked with providing recommendations on how the FIX Guidelines – which were already being leveraged in equity markets – could be utilised in post-trade processing for other major asset classes, including fixed income; equity swaps, equity options and foreign exchange (FX).

Having seen how FIX transformed trade execution [with 99.5% of trades now being carried out using the FIX standards], many in the industry believed FIX could be leveraged successfully in post-trade.

FIX MOVES INTO ETD POST-TRADE PROCESSING

Futures and options trading also faced significant challenges. The FIX Global Post-Trade Working Group noted that variations in workflows across multiple asset classes was causing serious problems, including frequent trade breaks and slow resolution times, which in turn was affecting margin calculations, creating risk and undermining client relationships.

Similar to other asset classes, post-trade processing for ETDs was manually intensive, with much of the repair and resolution work being undertaken by brokers. Other challenges also hindered trading in futures and options and impacted the post-trade process. For example, many global stock exchanges provided the executions fill-by-fill without an average price.

To overcome this, brokers would calculate an average price as part of the post-trade process. When asset managers would provide the brokers with the allocations for each trade, brokers had to develop their own best-fit algorithm so quantities were allocated fairly to the various accounts. Each broker typically had their own best-fit algorithm, which frequently made compliance and risk management teams at asset managers uncomfortable. As some of the larger asset managers have brought some of this function back in-house (computing the average price and allocating using a best-fit algorithm), brokers have faced



their own challenges which have resulted in inefficiency and exceptions. Conscious of these issues, the FIX Global Post-Trade Working Group sought out solutions.

The group published a standardised and comprehensive set of guidelines covering ETDs in 2016. The guidelines sought to iron out a number of the differences between these asset classes; “allowing connection to one or more third parties and/or intermediaries with the same protocol. With these guidelines, market participants will be able to reduce risk and have the ability to leverage off their current FIX infrastructure in place for trading – and by doing so – minimise implementation time costs,” according to a FIX statement.

The results for asset managers adopting these standards have been impressive.

Similar to other post-trade processes that have been automated via FIX, asset managers trading futures and options can now send their trades and allocations to the executing brokers, with the average price, who will have the information about the give-up or clearing brokers.

After the block level trade is matched by the executing broker, the allocations are sent via FIX to the clearing brokers.

The clearing broker will then generate confirmations based on the allocations and send them back to the asset manager.

At the point at which the asset manager receives the confirmation from the clearing broker, the matching process can begin, with exceptions identified in near real-time.

Exceptions can be resolved on trade date, thereby enabling trades to also be ready for settlement on trade date.

This has helped to eliminate many of the inefficiencies synonymous with post-trade’s manual processing, and it is delivering significant benefits to both asset managers and brokers.

MAKING IT HAPPEN

The asset management industry is facing a number of challenges today. Regulation has come in thick and fast since the 2008 financial crisis with rules such as AIFMD [Alternative Investment Fund Managers Directive] and MIFID II [Markets in Financial Instruments Directive II] all adding to asset managers' compliance costs.

Operating expenses are also rising, something which has been exacerbated by the pandemic. At the same time, clients are applying significant pressure on fees amid challenging performance conditions. With the industry looking to identify any cost savings, efficiencies gained in areas such as post-trade processing will help asset managers become leaner and more competitive.

This will be vital if managers are to win investor mandates moving forward in this highly competitive market.

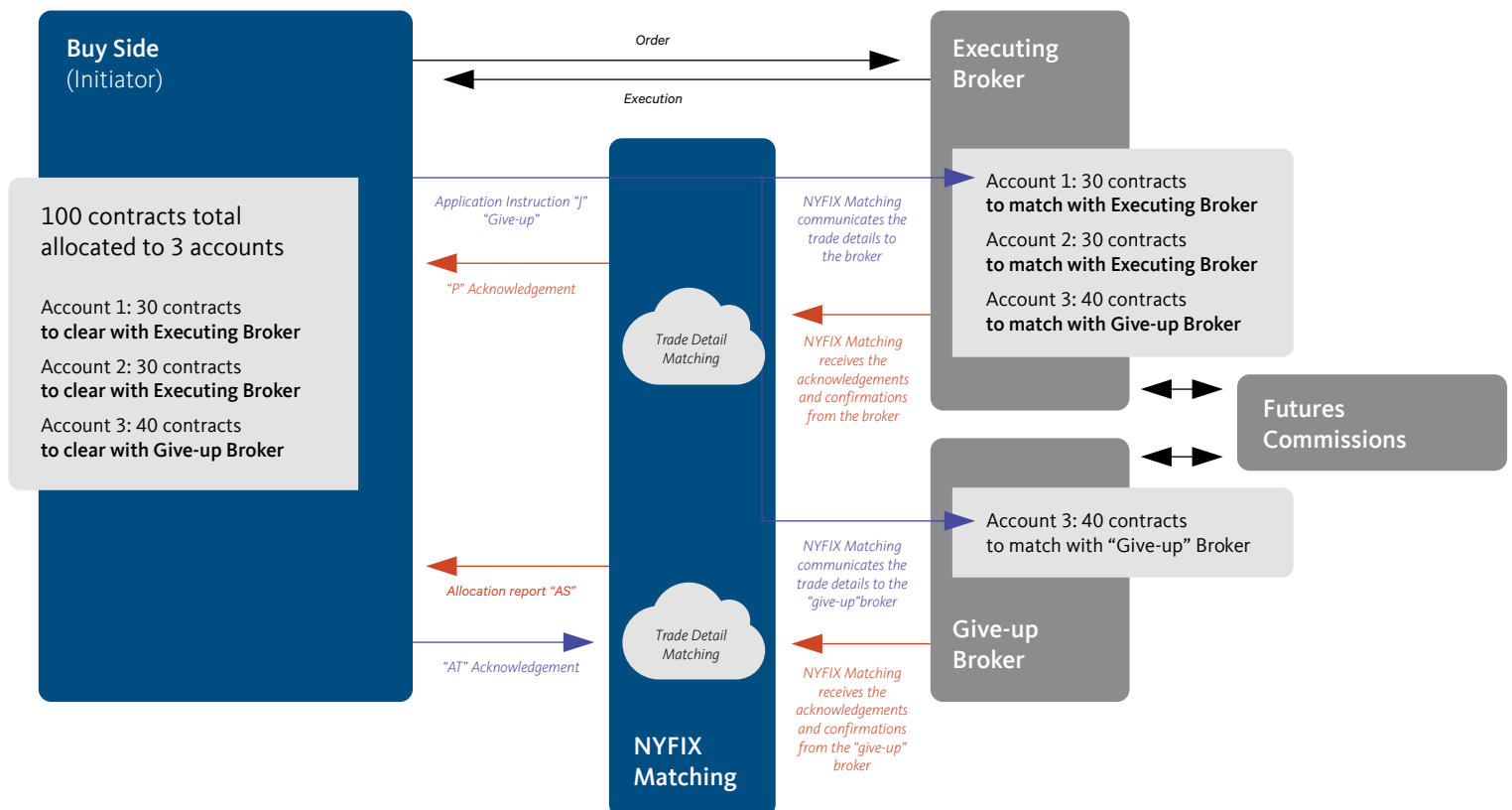
Broadridge's NYFIX Matching is a post-trade solution that can help with many of these challenges by streamlining post-trade processing across all asset classes.

Asset managers using NYFIX Matching can affirm, confirm and allocate trades with brokers through a FIX-based service that sits within one of the industry's largest networks for multi-asset trading, enables real-time matching supporting a faster settlement cycle, and helps reduce post-trade costs because of NYFIX's flat fee pricing model.

Enhancements to brokers' processes are also required if post-trade processing is to become more straightforward and efficient. Brokers have been responsible for handling a major portion of the very manual ETD post-trade process.

These firms have a number of people in the back office reviewing and processing post-trade exceptions so that trades settle on time.

Broadridge is in the process of integrating multiple products for the buy-side and the sell-side to provide a single end-to-end solution to the industry. This would bring efficiencies to post-trade processing and help to reduce processing costs.





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